

## Message Text

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SUBJECT: SECURITY SUPPORTING ASSISTANCE

1. BELOW IN PARA 2-9 IS TEXT OF SUBMISSION OF SECURITY SUPPORTING ASSISTANCE REQUEST TO BE SENT TO CONGRESS. THIS IS FYI ONLY, ALTHOUGH IT WILL EVENTUALLY BECOME PUBLIC DOCUMENT.
2. PURPOSE: TO PROVIDE THE GOVERNMENT OF TURKEY WITH IMMEDIATELY AVAILABLE FOREIGN EXCHANGE RESOURCES TO MEET SHORT TERM BALANCE OF PAYMENTS REQUIREMENTS.
3. FY 79 PROGRAM: IN ARRIVING AT THE FY 79 PROGRAM WE HAVE TAKEN INTO ACCOUNT TURKEY'S CAPABILITY TO UTILIZE THE FUNDS, IN CONJUNCTION WITH OTHER SOURCES OF ECONOMIC ASSIS-

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TANCE, SUCH AS BALANCE OF PAYMENTS SUPPORT FROM THE IMF, AND PROJECT-ORIENTED DEVELOPMENT AID. THE PROPOSED LOAN WILL BE EXTENDED FOR TEN YEARS INCLUDING THREE YEARS GRACE, WITH INTEREST AT COST OF BORROWING TO THE UNITED STATES TREASURY.

4. OVERVIEW: STRENGTHENING OUR BILATERAL RELATIONSHIP

WITH TURKEY IS A VITAL AND FUNDAMENTAL GOAL OF UNITED STATES POLICY IN THE EASTERN MEDITERRANEAN REGION. OUR COMMON SECURITY CONCERNS ARE AN IMPORTANT PART OF OUR EVOL-

VING RELATIONSHIP. IN ADDITION, TURKEY IS A MAJOR DEMOCRACY AS WELL AS A DEVELOPING COUNTRY, BOTH EUROPEAN AND ASIAN, WITH A ROLE IN THE WORLD AND IN THE STRATEGIC AREA OF THE EASTERN MEDITERRANEAN. AS PART OF ITS PROGRAM FOR REVITALIZING THE US/TURKISH RELATIONSHIP, THE ADMINISTRATION HAS PROPOSED THE REPEAL OF THE ARMS EMBARGO, ENACTED IN 1975 IN RESPONSE TO TURKISH ACTION ON CYPRUS IN 1974, SO THAT WE CAN MORE FULLY COOPERATE WITH TURKEY IN A MANNER CONSONANT WITH THE REQUIREMENTS OF AN ALLIANCE IMPORTANT TO OUR MUTUAL SECURITY. IN ADDITION, TURKEY IS PRESENTLY UNDERGOING SERIOUS ECONOMIC PROBLEMS, AND THE PROPOSED DOLS 50,000,000 LOAN WILL ASSIST TURKISH EFFORTS TO STABILIZE THE ECONOMIC SITUATION AS WELL AS PROVIDE A CONCRETE INDICATION OF OUR CONCERN FOR THE ECONOMIC PROBLEMS OF AN ALLY.

5. ECONOMIC OVERVIEW: TURKEY IS CURRENTLY GRAPPLING WITH SEVERE BALANCE OF PAYMENTS PROBLEMS WHICH HAVE SERIOUSLY WORSENERED DURING THE PAST YEAR. THE CAUSES INCLUDE INCREASED OIL PRICES, THE ECONOMIC SLOWDOWN IN WESTERN EUROPE WHICH ADVERSELY AFFECTED TURKEY'S EXPORT EARNINGS AND REMITTANCES BY TURKISH WORKERS, AND EFFORTS TO SUSTAIN LIMITED OFFICIAL USE

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RAPID ECONOMIC GROWTH THROUGH AN INVESTMENT PROGRAM WHICH DEPENDED ON IMPORTS OF CAPITAL AND INTERMEDIATE GOODS.

THE SUBSTANTIAL CURRENT ACCOUNT DEFICITS OF 1975-77 WERE INITIALLY FINANCED THROUGH A DRAWDOWN OF RESERVES AND BY SHORT-TERM BORROWING IN THE EUROMARKETS WHICH EVENTUALLY TOTALLED NEARLY DOLS 2 BILLION. BY EARLY 1977 THIS SOURCE OF FOREIGN CAPITAL HAD BEEN EXHAUSTED, AND THE CENTRAL BANK WAS UNABLE TO EFFECT TRANSFER OF FOREIGN EXCHANGE FOR ALL BUT THE MOST VITAL IMPORTS AND SOME DEBT SERVICE PAYMENTS. BY DECEMBER 31, 1977, TURKEY'S SHORT TERM EXTERNAL DEBT POSITION STOOD AT DOLS 5.4 BILLION.

IN SEPTEMBER 1977 THE GOVERNMENT INITIATED NEGOTIATIONS WITH THE IMF. AFTER A CHANGE IN GOVERNMENT IN JANUARY 1978, THE TURKISH GOVERNMENT SIGNED ON MARCH 23 A LETTER OF INTENT TO ENTER INTO A STANDBY AGREEMENT. (THE IMF BOARD IS EXPECTED TO APPROVE IT ON APRIL 24.)

6. CURRENT ECONOMIC SITUATION: 1977 WAS AN EXTREMELY DIFFICULT YEAR FOR THE TURKISH ECONOMY, AFTER YEARS OF STRONG GROWTH. THE PAYMENTS PROBLEMS CAUSED MANY FOREIGN

SUPPLIERS TO RESTRICT OR TERMINATE DELIVERIES TO TURKEY, AS DEBTS OWED TO THEM ROSE. SINCE THE TURKISH ECONOMY IS DEPENDENT UPON IMPORTED RAW MATERIALS, CAPITAL EQUIPMENT AND INTERMEDIATE GOODS, UNEMPLOYMENT ROSE RAPIDLY, REACH-

ING AN ESTIMATED 20 PERCENT, AND SHORTAGES CONTRIBUTED TO TRADITIONALLY HIGH INFLATION, DRIVING IT UP TO AN ESTIMATED 36 PERCENT ON AN ANNUAL BASIS BY THE END OF THE YEAR. NOTWITHSTANDING THE RESTRICTIONS BY FOREIGN SUPPLIERS, THE CURRENT ACCOUNT DEFICIT REACHED DOLS 3.4 BILLION IN 1977 (OIL IMPORTS TOTALLED SOME DOLS 1.8 BILLION) AS EXPORT RECEIPTS AND REMITTANCES BY TURKISH WORKERS FAILED TO GROW IN PROPORTION TO IMPORTS.

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A NUMBER OF MEASURES WERE TAKEN TO BRING THE ECONOMY UNDER CONTROL. TWO DEVALUATIONS, OF 9 PERCENT AND SUBSEQUENTLY IN EARLY 1978, 23 PERCENT WERE TAKEN, AND THE 1978 BUDGET CONTAINED REDUCTIONS, IN REAL TERMS, IN EXPENDITURES AND IN THE DEFICIT FROM 1977. SUBSTANTIAL PRICE INCREASES FOR THE PRODUCTS OF STATE ECONOMIC ENTERPRISES ARE EXPECTED TO REDUCE THEIR OPERATING DEFICITS, TRADITIONALLY FINANCED THROUGH THE BUDGET. PROCEDURES FOR EURODOLLAR BORROWING HAVE BEEN REVISED TO DETER ITS USE IN FINANCING SPECIFIC TRANSACTIONS AND TO BRING IT MORE UNDER CENTRAL BANK CONTROL. THE PROJECTIONS FOR 1978 NONETHELESS POINT TO A CURRENT ACCOUNT DEFICIT OF DOLS 1.5 BILLION, A SUBSTANTIAL REDUCTION FROM 1977, BUT IN CONJUNCTION WITH THE EXISTENT DEBT, A SIGNIFICANT PROBLEM.

7. ECONOMIC PROSPECTS: IN THE SHORT TERM, TURKEY'S ECONOMIC SITUATION WILL BE DIFFICULT. CONTINUED RESTRAINT ON GOVERNMENT EXPENDITURES, PARTICULARLY INVESTMENT, COULD AFFECT THE EXPECTED GROWTH IN STANDARD OF LIVING AND EMPLOYMENT LEVELS. THE ECONOMY WILL BE BURDENED BY ITS DEBT SERVICE OBLIGATION AS WELL AS BY THE COSTS OF THE INEVITABLE PROCESS OF ADJUSTMENT TO A MORE BALANCED ECONOMY. PRICES, PARTICULARLY OF STATE ENTERPRISE PRODUCTS, WILL CONTINUE TO RISE, ALBEIT LESS RAPIDLY THAN IN 1977, AND THE FULL IMPACT OF DEVALUATION ON PRICES WILL BE FELT DURING 1978. OPERATING IN A DEMOCRATIC SOCIETY, THE GOVERNMENT WILL HAVE THE DIFFICULT TASK OF MAINTAINING AUSTERITY IN A NATION ACCUSTOMED OVER THE PAST DECADE TO RAPID GROWTH. HOWEVER, WITH PER CAPITA INCOME AROUND DOLS 1,000, GOOD GEOGRAPHIC LOCATION, EXPLOITABLE NATURAL RESOURCES, (THOUGH DEFICIENT IN FOSSIL FUELS) AND A LARGE LABOR FORCE, MANY WITH EXPERIENCE ABROAD, TURKEY HAS LIMITED OFFICIAL USE

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BRIGHTER LONG-TERM PROSPECTS.

8. EXTERNAL DONOR ASSISTANCE: THE IBRD MAINTAINS A LONG-TERM PROGRAM IN TURKEY. SOME EUROPEAN STATES, NOTABLY THE FRG, HAVE PROVIDED BILATERAL ASSISTANCE. THE OECD CONSORTIUM FOR TURKEY WILL REVIEW THE TURKISH SITUATION DURING THE SPRING OF 1978. ASSUMING APPROVAL BY ITS BOARD OF DIRECTORS, THE IMF WILL BE PROVIDING APPROXIMATELY DOLS 450 MILLION IN THE NEXT TWO YEARS, AND TURKEY IS NEGOTIATING A REFINANCING OF ITS SHORT TERM DEBT WITH PRIVATE BANKS.

9. FY 1979 PROGRAM: A LOAN OF DOLS 50 MILLION IS PROPOSED FOR FY 1979. THIS LOAN WILL HAVE A BENEFICIAL, PRACTICAL IMPACT ON TURKEY'S EFFORTS TO STABILIZE HER ECONOMIC AND FINANCIAL SITUATION, AS WELL AS INDICATING CONTINUED US INTEREST IN THE ECONOMIC SITUATION OF A NATO ALLY AND OECD MEMBER STATE.

10. STATISTICAL PAGE WILL BE POUCHED. CHRISTOPHER

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